No. 11999

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

HARRY A. ROBERTS and RUTH M. ROBERTS,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONERS' BRIEF.

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Statement of Pleadings and Facts.

Petitioners allege:

1. That tips received by taxicab drivers are of the nature of gifts or gratuities and not taxable income.
2. That an arbitrary assessment of ten per cent of gross bookings of taxicab fare is unreasonable and cannot be supported under the evidence.

The answer consists largely of a general denial.

Decision was rendered by the Tax Court in favor of the Respondent.

Petitioners ask a review of such decision under the provisions of Section 1141-2 Internal Revenue Code.

Statement of the Case.

Harry A. Roberts, petitioner, a taxicab driver for the Yellow Cab Company in the year 1943, was notified by the Treasury Department under date of May 29, 1946, that his return for the taxable year 1943 showed a deficiency of $144.34, based upon an addition to his reported income of the amount of $661.94, representing tips which the Department asserts were received by him and which he failed to report in his return [Tr. 6]. The statement disclosed that his wages had been increased in the amount of $661.94 arbitrarily by the Department, the basis of said increase being ten per cent of the gross bookings of said Petitioner during said taxable year.

The petitioner during such year had kept no record of tips received by him [Tr. 24] admits that he received tips from his patrons from time to time [Tr. 24]; testified that only approximately fifty per cent of his patrons tipped at all and that in his opinion ten per cent of the fare received from those who did tip would be a fair estimate [Tr. 25].

The petitioner further testified that he rendered no services that were not comprehended within the fare as disclosed by the taxi-meter slip [Tr. 26], and that he had been advised by counsel that tips were not a part of his taxable income and accordingly [Tr. 24], the petitioner refused to pay the amount of the additional assessment.

Petitioner further testified that the basis of his employment was forty-five per cent of the "take," or Six Dollars

a day, which ever was greater [Tr. 27]. His testimony with reference to the size of the tips received from the passengers who do tip is as follows:

> ". . . for a 50-cent fare the usual "tip" was a dime [Tr. 27], on an 80-cent fare the usual "tip" was a dime [Tr. 29], on a dollar fare usually nothing [Tr. 29], on a 30-cent fare ten to fifteen cents [Tr. 29], on a $1.80 fare ten to fifteen to twenty cents [Tr. 32], and on the $10.00, $5.00 or $3.00 fare usually nothing; on charge accounts such as telephone companies, hospitals, Southern Pacific and Union Pacific Railroads and others, nothing [Tr. 32]; as to $10.00, $15.00 and $20.00 trips, probably one person out of twenty-five 'tips' " [Tr. 33].

P. C. Davis testified as follows:

> "That he had been employed in the Los Angeles area as a cab driver for the Yellow Cab Company for sixteen and one-half years [Tr. 34]; that he is the Chairman of a group of approximately 700 cab drivers [Tr. 40] and in such capacity was fully conversant with the problems involved here, namely the cab driver's relationship to his employer, the alleged 'custom of tipping,' the conditions obtaining in the Los Angeles area in 1943 and other years, the proportion of passengers who 'tipped.' In other words, Mr. Davis's statement of fact and opinion reflected a general study, at least to the extent of his observation and experience with seven hundred cab drivers, which summarily is as follows [Tr. 35-39]:
>
> That 40 to 50 per cent of cab passengers 'tip' [Tr. 36]; that no solicitation of tips is permitted by the employer or by the Board of Public Utilities [Tr. 36]; that there is no service rendered to a passenger not covered by the taximeter bill [Tr. 37]; that the

compensation of cab drivers is 40 to 45 per cent (depending upon seniority) of his bookings or $6.00 a day, whichever is the greater [Tr. 37]; that the amount of 'tip' is about 10 per cent of the fare of those who do 'tip' on an average [Tr. 38], and no tips whatever on charge accounts, which were numerous in the year 1943 [Tr. 39]; that on big trips, $5.00 to $20.00, those who did 'tip' would 'tip' less than the average, and pay at most 25¢ to 50¢ [Tr. 42[that he estimated the average cab driver would have one $10.00 trip per month and five or six $5.00 trips per month [Tr. 43].

The witness Davis further testified that after the government began demanding amended returns, he advised his group to keep a daily record; that on behalf of his organization he consulted counsel and received advice that in the opinion of counsel 'tips' constituted gifts and were not taxable income" [Tr. 40].

The Respondent's witnesses gave the following testimony:

"Orville Richardson, who worked as a cab driver in 1941 and 1942 and only one month in 1943 [Tr. 50] upon solely his personal record of 'tips' received by him, testified such 'tips' would average 10 per cent of bookings throughout the year; gave his opinion that such basis was conservative as relating to the average cab driver [Tr. 49].

"Respondent's witness, Lloyd E. Bryson, testified that it is a *custom* for a certain per cent of patrons to 'tip' [Tr. 52]; that approximately 50 per cent of patrons 'tip'; that the average person 'tips' because it is a 'custom' [Tr. 53] and on cross-examination testified that perhaps a little better than 50 per cent of the patrons 'tipped'" [Tr. 54].

"Herbert C. Hendrey testified that 50 per cent of his passengers 'tip'; that 10 per cent of gross 'take' in 1943 in his opinion is fair; a fair estimate in his case [Tr. 56-57]; that he would not say as to the average cab driver 'since there are so many things stipulate as to whether a cab driver gets a 'tip'" [Tr. 57]; that he never compared his 'tips' with other cab drivers and that he based his testimony solely upon his personal experience [Tr. 61], and that in 1943 he worked mostly in Beverly Hills" [Tr. 61].

In order to avoid the calling of many cab driver witnesses, respondent's counsel stipulated as follows:

"The Court: I will say now that I am not going to listen (57) to 20 cumulative witnesses.

"Mr. Hurley: I wish to say this, that in so far as taxicab drivers being forbidden to solicit tips, I am willing to stipulate to that. *I am willing to stipulate further that all the services are included in the fare,*" (Italics supplied.)

"Mr. Howard: We will accept the stipulation as presently stated by counsel.

"The Court: That settles that." [Tr. 47-48.]

Specifications of Error.

(1) Error in determining that petitioner's tips were taxable income in that they constituted compensation for services.

(2) The failure of the Court to determine that the rule of thumb of 10 per cent of gross "take" applied by the Commissioner by reason of the alleged failure of the taxpayers to keep adequate records, is arbitrary and unreasonable and is not supported by the great preponderance of the evidence.

ARGUMENT.

I.

An Arbitrary Assessment of 10 Per Cent of Gross Bookings as Constituting the Amount of Tips Received by Taxicab Drivers Is Unreasonable and Not Supported by the Evidence.

Under the evidence, without conflict, it appears that not all, but only approximately 50 per cent of taxicab patrons tip at all.

As to whether 10 per cent of gross bookings is fair, there is conflict. We submit, however, that the evidence preponderates greatly in support of petitioner's contention that should a rule of thumb be used, 10 per cent of the fare of those who do tip rather than 10 per cent of the gross "take" is the more reasonable.

Witness Roberts testified that he considered 10 per cent fair from those who did tip, since 10 per cent of 50 per cent [Tr. 26] is the average tip. The witness Davis, upon his own experience of sixteen and one-half years, and reflecting the opinion of an organization of seven hundred cab drivers, testified substantially the same [Tr. 38].

What is the respondent's evidence to the contrary? Orville Richardson testified that the tips would average at least 10 per cent of gross bookings throughout the year, based upon his purported personal records which were not produced [Tr. 49]. However, on cross-examination, he admitted that he worked only one month in the year 1943 [Tr. 50] so he could not have had records for the full year, thus his evidence is largely surmise as to 1943.

Respondent's witness, Monahan, was not queried on this issue. Respondent's witness, Bryson, gave 10 per cent of gross bookings as his estimate [Tr. 54]. Respondent's witness Hendrey (as to his experience only and not the average driver) opined that 10 per cent of bookings was fair [Tr. 57]; that he had no knowledge of other drivers' tips [Tr. 58] and worked chiefly out of the Beverly Hills office [Tr. 61].

P. C. Davis in such respect, however, testified that as to tips received by a driver working out of Beverly Hills, his tips would be approximately 25 to 30 per cent more than in other districts [Tr. 64].

Since it is undisputed that only 50 per cent of patrons tip, such arbitrary assessment would mean that the average tip received by the driver averages 20 per cent of the fare.

The *Cessaneli* case (8 P. C. 85), relied upon by the respondent in the trial court, wherein the Court held that an arbitrary assessment of 10 per cent of sales was justifiable under the evidence in such case, has little pertinency here.

The situation as to waiters may not automatically be extended to cover all vocations. Every day experience demonstrates that tipping of waiters exists to a much greater degree than tipping of cab drivers. A waiter can and oft times does render services not included in the bill —the extra glass of water, perhaps a clean cloth, a refill of one's coffee cup, help with one's coat at the conclusion of the meal and in a score of other respects. All that the taxicab driver does is to permit one to enter the vehicle, transport him to his destination and carry his bags, if any, all of which he is obligated to do for his employer and for which his employer pays him.

It is fundamental that an arbitrary assessment must be in consonance with reason. Since the Department made no effort prior to the year 1943 to require the inclusion of tips as income, we submit that a 10 per cent of gross bookings assessment by reason of the failure to keep records not previously required, is punitive.

II.

Tips Received by a Taxicab Driver Do Not Constitute Any Part of His Wages or Compensation for Services, but in Truth and Fact Are Gifts and Therefore Not Taxable Income.

The letter and spirit of the Income Tax Act is to impose a tax upon income and not upon gifts, unless the money allegedly "given" is in essence compensation for services.

The word "tip" or "tips" is not used in the Act itself; however, Regulations III, Sec. 29.22 (a-2) *Compensation for Personal Services,* includes the word "tips." Obviously, if the Commissioner went beyond the purview of the legislation, such regulation and all proceedings thereunder must fall.

Koshland v. Helvering, 298 U. S. 441;
Biddle v. Commissioner, 302 U. S. 573.

Gifts by the terms of the Act itself are made expressly exempt. Section 22 (b) (3) Internal Revenue Code.

What is the meaning of the word "tip"? Is it to be considered as a transaction constituting additional compensation for services rendered as claimed by the Department, or is it a gift or alms or the bestowment of moneys prompted by alleged custom, impelled by eleemosynary

or charitable feelings of the tipper, or for other reasons not constituting compensation?

Words must be construed and defined according to their true meaning; such is the purpose of language. To determine the true definition, one must at times seek the derivation or origin of the terms.

"Tips" in the sense of a small gratuity or present to an inferior, is probably derived from an old English verb to "tip" meaning to give (citing quotations back to the year 1610); (2) to give a gratuity to, to bestow—with a coin or sum of money as the object."—*The Oxford Dictionary:*

> "A small present of money . . .; a gratuity or fee . . ."

New Century Dictionary:

> "Noun—A sum of money given, as to a servant, usually to secure better or more prompt service. Verb—To bestow a gift or a gratuity of money upon, as a waiter or servant." *Funk & Wagnalls Unabridged Dictionary.*

Webster's Dictionary, as the trial court indicated, is not helpful since it tersely defines a tip as both a gift and a fee.

Among the references quoted in the Oxford Dictionary appears one from Thackary, as follows: "You used to tip me when I was a boy at school."

Again in *Notes and Queries,* 9th Series, Volume 4, page 352, citing Dr. Johnson, we find the following: "To tip —to give—a low cant term from the classical dictionary of the vulgar language."

Moreover, we find in Mr. George Simpson's book (published 1946) entitled *"A Book About a Thousand Things,"* page 242, the following analysis as to the origin of tips:

> "How did 'tip' originate? A curious story is told to account for the origin of tip in the sense of a small sum of money given for personal services rendered or expected. According to this story 'tip' was derived from the initial letters of the phrase 'to insure promptness.' Boxes in coffee houses were so lettered and later the phrase abbreviated to T. I. P., and from this circumstance, according to the story, *tip* and *tips* came into use. The quotations given in the Oxford Dictionary show the absurdity of this derivation."

And at page 462 of Notes and Queries above cited, a reading of J. Holden McMichaels' analysis effectively disposes of the coffee shop theory.

Although the issue in the case of *Herberts v. Laurel,* 58 Cal. App. 2d 684, has no application, since the question was whether tips constituted a part of the gross receipts of a business, the Court's definition of tip and the motive that impels it we deem most pertinent. We quote (page 694):

> "A tip is not intended for the proprietor of a restaurant; it is a gratuity, *i. e.,* a free gift, a present. *(28 C. J. 823.)* It is intended by the donor to be in excess of the compensation paid to the donee by the latter's employer or a gift where there is neither consideration for it nor a legal obligation upon the donor to part with it. *(Wellingham v. Drew,* 117 Georgia 850.) In the western world diverse motives incite the instincts of the tipper. With some, it is to gratify the charitable impulse; with others it is the desire for gratitude or esteem or arises from a zeal

> for extending one's good will. Still in others, the motive is to abide by an iniquitous practice under the compulsion of popular opinion. But whatever be the motive of the giver, his tip remains a gift to the donee. It cannot be fairly said that such gifts are intended to be additional compensation for the viands or liquids purchased from the restaurateur."

Nor can it be fairly said that such gifts are intended to be additional compensation for the taxicab ride.

The custom of tipping actually came into being long before the 16th Century. In England and on the Continent, such "gifts" were given as alms by the nobility to the subjects, serfs or inferiors, however denominated. In the early days, the lords, barons and knights would throw small coins to their inferiors. It was a customary gesture of the upper classes toward the lower classes. To say that a taxicab patron tips because it is a custom and perforce such tips are taxable, is erroneous. *We must determine whether it is a custom of paying or of giving.*

Regardless of our desire to believe that alms or gifts are *always* motivated by charitable impulses, such is not true. More often than otherwise, alms are given because John Doe did so, and to "save face," Peter Roe does likewise.

Another motivation is the desire of the bestower or tipper to demonstrate that the tippee is an inferior to the tipper.

The third analysis is that the tipper gives because he likes his fellow men.

Thus we see that the motivating impulse may be one or more of the following: A benevolent gesture indicating

the superiority of the donor; pure benevolence; or benevolence to "save face."

Respondent saw fit to introduce evidence in support of this latter concept:

> "Q. Mr. Bryson, when we discussed the matter prior to the trial of this proceeding, did you tell me that it was—you can answer this question yes or no—did you tell me that it was customary to tip, and as a matter of fact 'Most people would feel like a heel' to quote you, 'if they did not.'
>
> The Witness: There are personal reasons there.
>
> The Court: What is that?
>
> The Witness: It would be in personal cases. The average person, I would say, tips because it is a custom." [Tr. 51-53.]

Perhaps respondent's counsel is correct in such respect; doubtless many people permit benevolence to be impregnated with pride. Other persons give to indicate their importance and yet others are solely impelled by kindliness. As concerns the issue, however, what boots it? Under whatever conception, the transfer is still a gift and not compensation.

Intention is a state of mind. Since the donors were not available to testify as to their donative intent, we must rely upon such reasonable inferences as may properly be drawn from the testimony, the acts themselves, the true meaning of the term tip and the attributes of the custom.

Mertens in his Work *"The Law of Federal Income Taxation"* after reviewing the *Blair* case, 33 F. 2d 286, 279 U. S. 16, *Bogardus* case minority opinion, 302 U. S. 34,

82 L. Ed. 32 and *Rice,* 41 F. 2d 339, concludes (see Paragraph 808):

> "It is clear in these cases that the intention of the parties should control in determining whether the payment involved is a gift or compensation."

See also authorities collated 67 U. S. L. P. 548, 110 A. L. R. 285, 119 A. L. R. 418; *Helvering v. National Groceries,* 304 U. S. 282; *Helvering v. American Dental,* 318 U. S. 320; see also, *Mertens,* Para. 607, Page 246.

Aside from the ordinary rules of statutory interpretation, the basic authorities under the Income Tax Act defining income, with which the writer refrains from encumbering this brief, a search of the decided tax cases avails little.

The *Bateman* case (34 B. T. A. 351) cited by the trial judge in his opinion, definitely is not applicable here. There, under the undisputed evidence, payments were made to employees of transportation companies as an inducement

> "to load shipments of the Transcontinental Company and to expedite and facilitate the traffic so as to effect prompt delivery of such shipments. Payments were also made to passenger agents for sending prospective shippers to the Company." (p. 362.) "That the congested condition of traffic and transportation competition and shortage of cars in the years in question necessitated payments of varying amounts to employees of railroads and also industries; that it was a common practice; that it was necessary to obtain cars for their shipments and to move traffic." (p. 367.)

Perhaps the most comprehensive discussion of this subject appears in the *March, 1948* issue of *"Taxes"* in an article by George T. Altman and Harry Graham Balter, entitled *"Excludability of Tips as Gifts."* There these eminent tax authorities take this position:

> "It is not enough to say that tips are income; they must be taxable income and they are not taxable income if they fall within the scope of Sec. 22 (b)(3) (*i.e., gifts*). Citing *Bogardus v. The Commissioner,* 302 U. S. 34."

The testimony that all the services rendered by the cab drivers was covered by the fares is not controverted, all of the evidence on either side is to such effect. Moreover, respondent's counsel so stipulated in open court. [Tr. p. 47.]

Relative to the custom of tipping as being that of *paying* or *giving,* we submit that an exhaustive study lends no support to the conclusion reached by the trial court that it is compensatory. The trial judge's reasoning (in the opinion) that lessened service might result, should passengers cease tipping, and that the alleged gift being contemporaneous with the payment of fare demonstrates a payment for services, is not in consonance with the reasoning of the court in the case of *Helvering v. American Dental Co.,* 318 U. S. 322. An inducement necessarily precedes the act. The *Bogardus* case *supra,* draws a distinction between payment in consideration of services and payment in *appreciation* thereof.

Moreover, the conclusion reached in the trial court's opinion that the passenger tips because the taxicab driver expects to receive tips and the passenger expects to pay

something extra, is wholly unsupported under the evidence. Should we assume however that such inference might be drawn from the existence of a custom, it matters not. The compulsion of custom does not change a gift into a compensatory payment.

We suggest that the vast majority of people expect gifts for multifarious reasons or no reason at all. Similarly the donors expect to give. Mutual expectation cannot be considered the criterion, else we would be forced to conclude that a governmental agency might properly exceed the authority vested in it by Congress and hamstring all kindliness, all benevolence and all material expressions of appreciation.

Conclusion.

We respectfully urge that the determination of the trial court that petitioner's tips constitute taxable income should be held erroneous.

Without detracting from our chief position, we urge that should this Court rule adversely to us in the foregoing respect, the arbitrary assessment sustained by the trial court be held insupportable under the record in this cause.

Respectfully submitted,

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